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C O N F I D E N T I A L SECTION 01 OF 02 HONG KONG 000540

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STATE FOR EAP/CM AND EEB/IFD/OIA, TREASURY FOR JOHN HARRINGTON, EMBASSY PARIS FOR USOECD O'REILLY

E.O. 12958: DECL: 03/20/2024
TAGS: EFIN ECON HK CH SG
SUBJECT: HK HOPES TAX AMENDMENTS WILL BOOST INVESTMENT, AVOID EMBARRASSMENT

REF: HONG KONG 40

Classified By: Consul General Joe Donovan, Reason 1.4 b/d

¶1. (C) Summary: Hong Kong officials have been closely watching moves against jurisdictions accused of facilitating tax evasion. They hope a proposal to liberalize the exchange of tax information will facilitate double taxation agreement negotiations and keep Hong Kong out of international tax collectors' sights. Senior government officials emphasize that meeting the OECD 2004 Exchange of Information standards will boost Hong Kong's competitiveness and its ability to attract international investment. The government currently is discussing the proposal with Hong Kong's Legislative Council; the legislation is expected to pass by the middle of ¶2009. End Summary.

¶2. (C) Comment: The government has publicly underlined the potential benefits for investment, competitiveness, and its desire to adopt internationally recognized standards. But privately, officials are clearly concerned that without amending the law, Hong Kong could face the embarrassment of being included on "official" lists of tax havens or even be the target of future sanctions. Senior Financial Services and Treasury officials were extremely familiar with the details of the 2007 "Stop Tax Haven Abuse" bill sponsored by Senators Levin, Coleman and Obama and Senator Levin's recent proposal to resubmit an expanded version of the 2007 bill, and were eager for confirmation that passage of these new measures would "get them off the tax haven lists." End Comment.

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Adopting OECD EoI Standard to Boost Competitiveness
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¶3. (SBU) Hong Kong Financial Secretary John Tsang announced during his February 25 budget speech that the government will propose amendments to Hong Kong law that will allow it to meet OECD 2004 standards for exchange of tax information (EoI). The new law will allow Hong Kong's Inland Revenue Department (IRD) to gather and share information requested in specific cases by agreement partners even if it is not normally collected for Hong Kong's own tax purposes. Hong Kong Permanent Secretary for Financial Services and the Treasury Clement Leung said these amendments are necessary to allow the Hong Kong government (HKG) to negotiate additional double taxation agreements and encourage investment in the Hong Kong Special Administrative Region (HK SAR). Officials believe Hong Kong's current legislation, which is compliant with OECD 1995 standards, is no longer up-to-date and has become an obstacle to Hong Kong's investment competitiveness.

¶4. (SBU) Leung noted that Hong Kong had held public consultations on a proposal to adopt the 2004 OECD recommendations in 2005. The public was evenly split on the issue at that time, with many concerned that adopting the more liberal exchange of information standards would compromise taxpayer privacy and pose an undue burden on HKG resources. But in the past four years, said Leung, many of Hong Kong's major trading partners have adopted the new standard. Although Hong Kong already has negotiated five double taxation agreements and signed one with Vietnam last year, these are all based on 1995 OECD exchange of information provisions. Other trading partners are unwilling to negotiate with Hong Kong until it adopts the 2004 recommendations.

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If Others Can Do It...
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¶5. (SBU) Seeing many of their major trading partners adopting the more liberal standard, the government again engaged the public on the issue in May 2008. The example from other tax jurisdictions has clearly reassured the doubters, said Leung. Most now support amending Hong Kong law to bring the SAR into compliance. Concerns that adopting the newer standard would disadvantage Hong Kong vis--vis Singapore were laid to rest when Singapore announced it would also adopt the OECD 2004 standard. Hong Kong officials have consulted extensively with the Hong Kong Privacy Commission to reassure them that any proposed amendments will protect public information and will not allow "fishing" for

incriminating data.

¶6. (SBU) The Hong Kong Financial Services and Treasury Bureau is currently discussing the Government's budget proposal with Legislative Council (Legco) members, who have submitted over 3,000 written questions, said Leung. He expected discussions on the proposed amendments to the exchange of tax information laws will continue for the next several weeks, with specific legislation submitted to the Legco by mid-summer 2009. The proposal is not controversial, he said, and is expected to pass without difficulty. Hong Kong officials hope the amendments will be passed quickly so they can get to work approaching their top trading partners to gauge their interest in negotiating double taxation agreements. Once Hong Kong is OECD 2004 compliant, said Leung, the government should be able to quickly sign agreements with several key trading partners.

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Hong Kong Seeks Chinese Level of Certainty
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¶7. (C) Officials believe the time is ripe for Hong Kong to amend its law to bring it into compliance with the globally recognized standard. Investors in Hong Kong will benefit from increased certainty, said Leung. In recent years, outside investors have complained to the HKG that the lack of double taxation agreements increases confusion and the potential for falling afoul of their own domestic tax authorities. Even China has a broad network of double taxation agreements (although not OECD 2004 compliant) that clarify business tax obligations. Leung said his office has been approached by Chinese investors in some sectors who prefer not to move their operations to Hong Kong because their tax liabilities in China are more transparent.

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Hong Kong no Tax Haven, Say Officials
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¶8. (C) Leung said he was surprised by the Government of Singapore's announcement that it would also revise its law to

allow it to sign OECD 2004 compliant double taxation agreements. Many in Hong Kong had cited Singapore's reluctance to do so as a reason to delay revising Hong Kong's law (reftel). Hong Kong's action may have pushed Singapore to move more quickly than officials there had planned, said Leung. Principal Assistant Secretary Cheng added that Hong Kong has been closely monitoring international pressure on jurisdictions considered to be "tax havens." Hong Kong and Singapore have been included on several lists of jurisdictions accused of being tax havens, said Leung, including a December 2008 U.S. Government Accountability Office (GAO) Report identifying large U.S. corporations and Federal contractors with subsidiaries in "Tax Havens or Financial Privacy Jurisdictions."

¶9. (C) Leung and Cheng noted that there is disagreement about what constitutes a tax haven and contested the GAO's methodology. Hong Kong's low tax rate makes it an attractive place to do business, but it has no tradition of bank secrecy and the authorities have cooperated with efforts to prevent tax evasion, said Cheng. The OECD does not consider Hong Kong a tax haven, he added. Nevertheless, Hong Kong has been trying to correct the impression that HK SAR regulations encourage tax evaders to set up shop. The Hong Kong Economic and Trade Office (HKETO) has been reaching out to Congressional staff to educate them on Hong Kong's law, said Cheng.
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